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In the Supreme Court

CHARLES ELMORE CROPLEY
CLERK

OF THE

United States

OCTOBER TERM, 1943

No. 420

THE AMERICAN DISTILLING COMPANY,
Petitioner,

vs.

LOS ANGELES WAREHOUSE COMPANY,
Respondent.

**PETITION FOR WRIT OF CERTIORARI
to the Supreme Court of the State of California
and
BRIEF IN SUPPORT THEREOF.**

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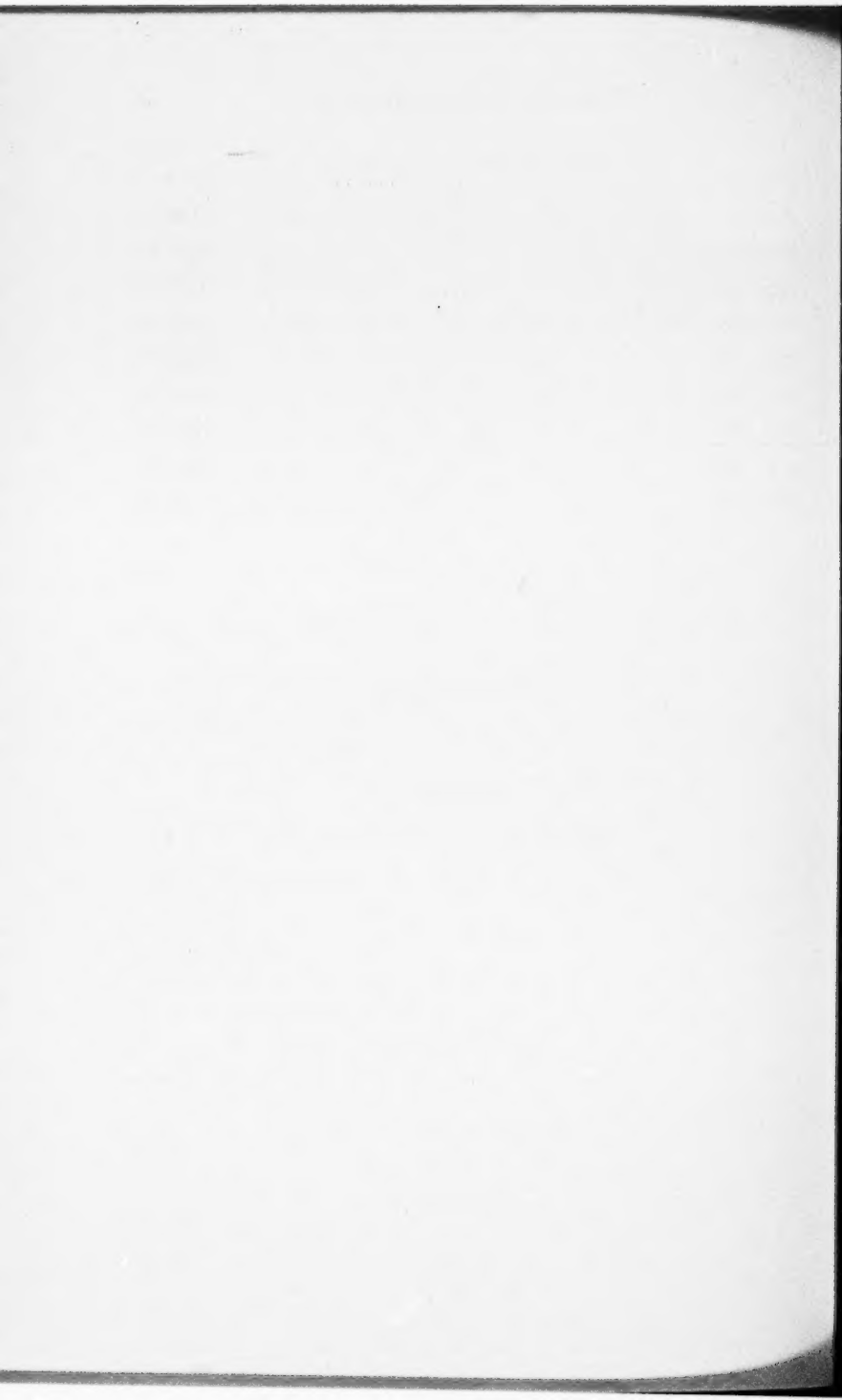
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LOS ANGELES WAREHOUSE COMPANY,
Respondent.

PETITION FOR WRIT OF CERTIORARI to the Supreme Court of the State of California.

*To the Honorable Harlan Fiske Stone, Chief Justice
of the United States and to the Associate Justices
of the Supreme Court of the United States:*

Petitioner, the American Distilling Company, respectfully prays that a writ of certiorari issue to review a decision of the Supreme Court of the State of California rendered on June 30, 1943 (R. 172) and which became final on the 30th day of July, 1943. This Court on September 20, 1943, extended the time to file this petition until October 15, 1943. (R. 173.)

**SUMMARY AND SHORT STATEMENT OF THE
MATTER INVOLVED.**

Los Angeles Warehouse Company, hereinafter referred to as plaintiff, operates a United States bonded warehouse in Los Angeles. (R. 16.) The American Distilling Company, hereinafter referred to as defendant, operates a distillery in Sausalito, Northern California, and at the same place a United States bonded warehouse. (R. 16.) San Angelo Corporation, hereinafter referred to as San Angelo, is in the wholesale liquor business in Los Angeles and a warehouse customer of plaintiff. San Angelo ordered from defendant 25 drums of gin in bond to be delivered to plaintiff's bonded warehouse. (R. 17.) Pursuant to regulations issued under authority of federal statutes, plaintiff made application to the Department of Internal Revenue on a form known as 236 for a permit for the gin to be moved in bond by Evans Freight Lines, a highway motor carrier, from defendant's bonded warehouse to plaintiff's bonded warehouse. (R. 17.) A permit was so issued, and while in transit an accident occurred as a result of which the gin was destroyed by fire. (R. 19.)

The liquor was destroyed (removed from bond) under circumstances that the government became entitled to the tax. (R. 37, 19.) Liability for the payment of the tax is specifically covered by plaintiff's bond, furnished to qualify it to do business as an internal revenue bonded warehouse. (R. 7-10.) The Collector of Internal Revenue demanded payment of the tax from plaintiff, the receiving bonded warehouse. (R. 33.) No demand was made upon defendant. (R.

32-33.) Plaintiff paid the tax and brought this action against defendant for reimbursement. The trial Court rendered judgment in favor of plaintiff. This was affirmed by the District Court of Appeal. A hearing was granted by the State Supreme Court, which affirmed the judgment, the members of the Court, however, disagreeing radically on the grounds for the affirmance.

All essential facts are contained in an agreed statement. (R. 15.) It is stipulated that under the federal statutes and regulations distilled spirits in transit from one bonded warehouse to another are from the time of leaving the forwarding bonded warehouse deemed to be in the possession and custody of the receiving bonded warehouse and covered by its bond. (R. 17.)

Four of the justices of the State Supreme Court held that the internal revenue tax is a property tax, follows the property, is included as a part of the value of the goods, and on their accidental destruction while in bond the owner must pay the tax as an incident of ownership. (R. 165.) Three of the justices took definite issue with the theory that under the federal laws the tax on distilled spirits is a property tax and becomes a liability of the owner as an incident of ownership, and affirmed the judgment on the theory that under the federal laws and regulations the distiller remains primarily liable for the tax, notwithstanding the distilled spirits have passed into the custody of a bonded warehouse. The minority held that under the federal statutes and regulations, in the event of loss or destruction of distilled spirits, while in

the custody and covered by the bond of a bonded warehouse, the distiller, and not the bonded warehouse, is primarily liable and must bear the loss. (R. 169.)

THE QUESTIONS PRESENTED.

The questions presented are the following:

1. Is the internal revenue tax on distilled spirits a property tax for which the owner of the liquor in bond becomes personally responsible as an incident of ownership? Specifically, if distilled spirits are accidentally lost or destroyed while in bond (in the custody of a United States Internal Revenue bonded warehouse) under circumstances that the tax thereon becomes due to the government, is the owner of the liquor, by virtue of the fact of ownership, obligated to reimburse the bonded warehouse in whose custody the spirits were at the time of destruction and from which the government demanded and collected payment of the tax?

2. Is the distiller or the internal revenue bonded warehouse in possession primarily liable for the payment of the internal revenue tax on distilled spirits accidentally destroyed while in the custody, and covered by the bond, of the warehouse?

**BASIS OF JURISDICTION OF THE SUPREME COURT
OF THE UNITED STATES.**

This case presents the issue of primary responsibility under federal statutes for the payment of the tax on distilled spirits, when such tax becomes due by reason of the accidental destruction of the spirits while in bond and in the custody of a United States bonded warehouse. The statutes and regulations involved are set forth in an appendix to this petition. The pleadings, the agreed statement of facts and the opinions of the Courts below, show that the federal questions presented by this petition were there raised and decided adversely to petitioner.

The appeal was first heard by the District Court of Appeal of the State of California. (R. 157.) That Court concluded that under the federal statutes primary and ultimate liability for the tax is at all times on the distiller and that collection is made from the bonded warehouse by the government as a matter of administrative convenience:

"On this appeal defendant urges that under the provisions of the law, and the regulations made thereunder, when bonded liquor is damaged or destroyed in transit, the primary obligation is upon the receiving warehouse, and that the owner or distiller is not liable, except secondarily, for such tax. * * * From the above analysis it follows that as between the receiving warehouse and the distiller the ultimate and fundamental responsibility rests upon the distiller. * * * When plaintiff paid the tax, as it was required to do, it was not paying its debt, but the debt of defendant. Plaintiff's primary responsibility to the Govern-

ment for the tax was simply the result of Congress' attempt to facilitate the administration of the tax provisions and the collection of the tax." (R. 160, 164.)

The majority, four, of the State Supreme Court, interpreted the internal revenue statutes imposing taxes on distilled spirits as a property tax, a tax on the goods themselves, and construed payment to be an obligation incident to ownership of the liquor:

"Defendant contends the Internal Revenue Code and regulations of the Department of Internal Revenue places primary (and inferentially ultimate) responsibility upon plaintiff for payment of the tax, and that to hold the distiller liable therefor would place upon the latter an impossibly burdensome contingent liability should gin distilled by it be destroyed after such gin had passed out of its control. It is not as the distiller, however, but rather as the *owner* of the gin that defendant here must reimburse plaintiff. The *owner* of the liquor lost it when it burned, and he must bear the loss of its total value, which, as we have seen, includes the tax which had attached. If title had passed from defendant company to its customer, then such loss, in the absence of some other controlling circumstance, would have been upon the customer rather than upon defendant.
* * *

Inherently the tax is imposed on the *goods*, not on the manufacturer or the bailee. So far as persons dealing with the liquor are concerned the *tax follows the property as a necessarily included part of the value thereof* and, hence its actual payment being merely deferred, it becomes an

obligation of the owner, as an incident of ownership, payable on removal from bond.” (Italics as in opinion.) (R. 167, 169.)

The minority, three, of the State Supreme Court disagreed with the majority, and stated the issue as follows:

“I concur in the result reached in the majority opinion but do not agree that the federal excise tax on distilled spirits is a property tax, that the tax follows the property ‘as a necessarily included part of the value thereof,’ or that it ‘becomes an obligation of the owner, as an incident of ownership’. To employ property law concepts in the solution of problems like the present one can lead only to confusion.

The issue turns not upon who had title to the liquor that was destroyed, but upon whose tax liability was discharged by plaintiff when it paid the tax after the destruction of the liquor. * * * The determination of this issue rests upon the proper interpretation of the federal statutes and regulations with respect to the federal excise tax on distilled spirits. * * *

These provisions impose an excise tax on distilled spirits measured by the quantity distilled. (*United States v. Singer*, 82 U.S. (11 Wall.) 111, 121 (21 L. Ed. 49); see *Patton v. Brady*, 184 U.S. 608 (22 S.Ct. 493, 46 L.Ed. 713)). * * * If the tax were a property tax it would have to be apportioned among the states according to population. (U.S. Const. art. 1, sec. 2; see *Bromley v. McCaughn*, 280 U.S. 124 (50 S.Ct. 46, 74 L.Ed. 226); *Pollock v. Farmer’s Loan & Trust Co.*, 157 U.S. 429 (15 S.Ct. 673, 39 L.Ed. 759).)” (R. 169-170.)

If the tax on distilled spirits is not a property tax, which the owner of the liquor is personally obligated to pay as an incident of ownership, then the decision of the majority of the State Supreme Court is erroneous. If, as between the distiller and the bonded warehouse having custody of the liquor, the primary liability under federal statutes and regulations for the payment of the tax on spirits destroyed while in the custody of the warehouse, is on the internal revenue bonded warehouse, then the decision of the minority is erroneous.

Federal questions are presented and this Court has jurisdiction to hear and grant this petition under section 237, Judicial Code (28 U.S.C.A. 344b).

REASONS RELIED ON FOR ALLOWANCE OF WRIT.

This case falls directly within subdivision (a), Section 5, Rule 38. "A State Court has decided a federal question of substance not theretofore determined by this Court." This Court has not heretofore had occasion to determine the questions presented by this petition, and they come before it as matters of first impression.

Majority opinion.

No Court, so far as we have been able to ascertain, has heretofore construed the internal revenue tax on distilled spirits to be a property tax, or a tax which the owner of the liquor is personally obligated to pay as an incident of ownership. No authority for this construction is cited in the opinion.

The minority criticism, that if the tax on distilled spirits were a property tax it would be a direct tax and levied in violation of article 1, section 2 of the Constitution, is sound.

Bromley v. McCaughn, 280 U.S. 124, 74 L. Ed. 226;

Pollock v. Farmer's Loan & Trust Co., 157 U.S. 429, 39 L. Ed. 759;

Dawson v. Kentucky Distillery & Warehouse Co., 255 U.S. 288, 65 L. Ed. 638.

There is nothing in the federal statutes or regulations that in the slightest degree implies a personal liability for the payment of the tax on the owner of the liquor in bond. Title is vested in the owner subject to the lien of the government for the payment of the tax. Possession can only be acquired by payment, but there is no personal obligation or liability on the owner.

The assumption that the tax is included as a part of the value of the liquor in bond, and that on its destruction the owner's loss is equivalent to the value of the liquor tax paid, is unsound. Likewise, is the deduction from this premise that the owner must reimburse the bonded warehouse in possession for the amount of the tax, on the theory that "if the subject of bailment perishes or is lost, or is destroyed or damaged by accident, without any fault on the part of the bailee, the loss must fall on the bailor". The opinion draws no distinction between the rights and liabilities of the owner of liquor in bond (in the custody of an internal revenue bonded warehouse and subject to tax) and

the owner of tax paid liquor on deposit in an ordinary warehouse. The rights and liabilities of the owner, as well as the obligations and duties assumed by the warehouse, are fundamentally different in the two cases. The bonded warehouse has assumed certain obligations specifically covered by its bond to the government, as a condition to the privilege of operating as such. One of these obligations is to pay the tax if the liquor is withdrawn from bond by loss or destruction, under circumstances that the statutes do not provide for the remission of the tax.

The payment of the tax is deferred while the liquor is in bond. The owner cannot obtain possession without payment of the tax. It is, however, quite a different matter to be obliged to pay the tax without getting the liquor. If the majority opinion is correct, any one who purchases and owns liquor in bond faces a personal liability to pay the tax in the event of its removal from bond by accidental loss or destruction. It would be extremely hazardous to own liquor in bond. The amount of the tax is several times the intrinsic value of the liquor itself. If in this particular case title had passed to San Angelo (if, for example, the contract between San Angelo and defendant had provided for delivery f.o.b. defendant's warehouse) then San Angelo as the legal owner, would have been liable to plaintiff for the tax. "If title had passed from defendant company to its customer, then such loss, in the absence of some other controlling circumstance, would have been upon the customer rather than upon defendant". (R. 168.) The fact that the defendant

happened to be the distiller and also owner of the forwarding warehouse is wholly coincidental and plays no part whatsoever in the majority opinion. "It is not as the distiller, however, but rather as the *owner* of the gin that defendant here must reimburse plaintiff". (R. 167.)

Although the owner has no right of access to the liquor or to watch or guard it while it is in bond, and possession and custody are exclusively vested in the licensed bonded warehouse, the owner would nevertheless be responsible for the tax on the liquor, where lost or destroyed under circumstances that negligence on the part of the warehouseman could not be established. On the other hand, the warehouseman, who has qualified to serve as the custodian of the liquor on behalf of the government while it remains in bond, and incidentally is entitled to charge the public for this accommodation, can look to the owner for reimbursement in the event of its accidental loss or destruction while in his possession.

The liquor tax is not a property tax, but an excise tax.

Patton v. Brady, 184 U.S. 608, 46 L. Ed. 713, 717-719;

United States v. Singer, 82 U.S. 111, 121, 21 L. Ed. 49, 57.

The payment of the tax is secured to the government by a personal obligation on the part of the manufacturer covered by the manufacturer's bond, by a personal obligation on the part of the internal revenue

bonded warehouse in possession covered by the warehouseman's bond, and by a lien on the liquor itself. The majority conclusion that ownership of the liquor in bond entails a personal liability for the tax is fallacious. It is important that this issue be determined by this Honorable Court.

Minority opinion.

The minority concludes that under the federal statutes and regulations, the liability of the internal revenue bonded warehouse, to pay the tax on liquor lost or destroyed while in its custody, is ancillary to and by way of security of the distiller's obligation. (R. 17f) It will be observed that no authority or precedent is cited for this conclusion. It purports to be an original deduction from an analysis of the statutes.

As a matter of fact, the determination is in conflict with the decision of the Treasury Department, charged with the enforcement of law, and two decisions of the United States Circuit Court of Appeals.

Treasury Decision No. 20,290 (see appendix) was issued in answer to the inquiry whether any liability whatsoever rests under a distiller's bond after the distilled spirits have been deposited in a bonded warehouse and are covered by a warehousing bond. The decision was that, while liability remains under a distiller's bond, resort should only be had thereto after the warehousing bond has been exhausted. This ruling necessarily implies that primary responsibility rests on the bonded warehouse for loss that is covered by

its bond. This decision was rendered in 1899 and has ever since governed the practice of the department.

In *United States v. Guest*, 143 Fed. 456, the Circuit Court of Appeals of the Fourth Circuit definitely held that the sureties on the distiller's bond are secondarily liable and those on the warehouseman's bond primarily liable, in the event of a tax liability covered by the warehousing bond. The Court held that *manifestly* primary responsibility rests under the warehouse bond and the sureties on the distiller's bond, "if at all, are only secondarily liable."

In *United States v. National Surety Company of Kansas City*, 122 Fed. 904, the Circuit Court of Appeals of the Sixth Circuit cites and approves Treasury Decision 20,290, that the warehousing bond must be exhausted before resort is had to the distiller's bond.

The minority decision would make the distiller primarily liable for the tax on all distilled spirits manufactured and sold in bond. Having no knowledge of the ownership or location of spirits once sold, no control or check on the place where stored or the means of transportation employed, the distiller would never know from what corner of the country demands might come for payment of taxes on liquor for which, when sold, it had received the intrinsic or in bond price.¹ If such were the law, the only safe manner

¹Such was the basis of the sale in this case. The selling price was \$.28 per proof gallon delivered Los Angeles. (R. 18.) The tax was then \$2.25 per gallon, approximately eight times the selling price. The tax has since been increased to \$6.00 per gallon, approximately twenty-eight times the selling price in this case.

in which a distiller could operate would be to pay the tax in all instances and sell the liquor tax paid. This, however, would frustrate the very purpose for which the bonded warehouses were created. This question is also one that should be decided by this Honorable Court.

PRAYER.

Wherefore, petitioner prays that a writ of certiorari be issued out of and under the seal of this Honorable Court directed to the Supreme Court of the State of California, commanding that Court to certify and send to this Court for its review and determination, on a day certain to be therein named, a full and complete transcript of the record and of all proceedings in the case entitled Los Angeles Warehouse Company, Plaintiff and Respondent, v. The American Distilling Company, Defendant and Appellant, and being No. 12066 of the records of said Court, to the end that said cause may be reviewed and determined by this Honorable Court as provided by the statutes of the United States, and for such other and further relief as may be proper.

Dated, San Francisco, California,
October 4, 1943.

THEODORE H. ROCHE,
Attorney for Petitioner.

NORMAN A. EISNER,
Of Counsel.

In the Supreme Court

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OCTOBER TERM, 1943

No.

THE AMERICAN DISTILLING COMPANY,
Petitioner,

vs.

LOS ANGELES WAREHOUSE COMPANY,
Respondent.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

OPINIONS OF THE COURTS BELOW.

The opinion of the District Court of Appeal is reported in 55 A. C. A. (Advance Cal. App. Rep.) page 52, and appears in the record at page 157. The opinion of the Supreme Court of California is reported in 22 A. C. (Advance Cal. Rep.) page 413, and appears in the record at page 165.

JURISDICTION.

A statement of the basis on which this Court has jurisdiction to grant the writ, is set forth at page 5 of the petition.

STATEMENT OF THE CASE.

For the purposes hereof petitioner relies upon the statement of the case on pages 2 to 4, inclusive, of the petition herewith.

SPECIFICATIONS OF ERRORS.

Petitioner submits that the Supreme Court of the State of California erred in the following particulars:

1. In holding that the federal tax on distilled spirits is a property tax.
2. In holding that the owner of distilled spirits in bond becomes personally liable for the payment of the tax as an incident of ownership.
3. In holding that the owner of distilled spirits in bond must reimburse the internal revenue bonded warehouse, which was in possession of the liquor at the time of its accidental destruction, for the amount of the internal revenue tax on the destroyed liquor that the bonded warehouse has been required to pay under its bond to the Government.
4. In holding that as between the distiller and internal revenue bonded warehouse in possession of distilled spirits, the distiller is primarily liable for the

internal revenue tax on distilled spirits removed from bond by accidental destruction while in the custody of the bonded warehouse.

FEDERAL STATUTES AND REGULATIONS INVOLVED.

The statutes and regulations involved have been printed in an appendix.

Attention is respectfully directed to the following facts:

1. There is nothing in the statutes or regulations that so much as suggests a personal liability on the owner of liquor in bond.

2. The distiller is required to file a bond in a penal sum not less than the amount of tax on the spirits that can be distilled in his distillery during a period of fifteen days, but in no case in excess of \$100,000.00. (I. R. C. §2814.)¹

3. Each internal revenue bonded warehouse is required to file a bond to guarantee payment of the taxes, in an amount not in excess of \$200,000.00. (Double the maximum amount of the distiller's bond.) (I. R. C. § 2879.)

4. After manufacture, the spirits may be placed in internal revenue bonded warehouses and the payment of the tax deferred for a maximum period of eight years. The liquor may be transferred from one bonded

¹The references are to sections of the Internal Revenue Code and regulations set forth in the appendix.

warehouse to another and may be freely traded in while in bond. (I. R. C. § 2879; Reg. pars. 95, 102.)

5. The internal revenue bonded warehouse in custody is made directly liable for the payment of the tax on its removal from bond. (This includes removal by destruction, loss, theft or under any circumstances that the tax is not remitted.) (I. R. C. §§2879, 2880; Reg. pars. 44, 50, 68, 70, 118, 119, 130.)

6. When distilled spirits are transferred in bond from one bonded warehouse to another, the receiving bonded warehouse is made responsible and the liquor is deemed to be in its custody and covered by its bond during transfer. (Reg. par. 44.)

7. For the protection of the receiving bonded warehouse, the spirits can only be moved to its premises on its application and by a means of transportation and carrier designated by such receiving warehouse. This application is made on Form 236. A copy of Form 236 filled out by the plaintiff as receiving warehouse in this case is annexed to the amended complaint. (R. 6A.) (Reg. pars. 103, 113.)

8. There is no provision that the distiller shall be notified of transfer from one bonded warehouse to another (either before or after transfer) or that the distiller shall have anything to say respecting the carrier or means of transfer.

9. While as a practical matter the owner of the distilled spirits would undoubtedly know of the transfer of his liquor from one bonded warehouse to another, and would also be interested in knowing the

carrier or means of transportation employed, there is no provision in statute or regulation requiring that the owner be notified or consulted pertaining to the carrier or means of transportation designated by the receiving bonded warehouse.

10. If the license of a bonded warehouse in which liquor is stored is revoked, the owner of the liquor is required to move it to another bonded warehouse in good standing, and if he does not do so, the liquor is subject to seizure and sale for the payment of taxes thereon and costs and expenses of sale and removal. This is the only duty imposed on the owner by statute or regulation. It implies the very opposite of a personal liability. There is only the right to resort to the liquor itself. (I. R. C. §2874, Reg. par. 120.)

ARGUMENT.

The majority opinion is erroneous for the following reasons:

(a) It places on every owner of liquor in bond a personal liability for the payment of the internal revenue tax thereon, in the event of its accidental loss or destruction while in bond.

(b) It erroneously construes the internal revenue tax to be a property tax, payment of which the owner of the property assumes as an incident of ownership.

(c) It erroneously assumes the value of liquor in bond to the owner to be its value tax paid.

(d) It erroneously concludes, from the false premise (c) and upon the principle, that as between an innocent bailor and bailee, the bailor must bear the loss of the property, that the owner of the liquor in bond as bailor must reimburse the internal revenue bonded warehouse as bailee for the tax on the liquor as a part of the value of the property lost or destroyed.

The minority opinion is erroneous for the following reasons:

(a) It would place upon the distiller ultimate liability for the payment of the internal revenue taxes on all liquor manufactured and sold in bond. The distiller, however, after having sold the liquor in bond for its intrinsic value and subject to tax, loses all contact with or control over the liquor. It is thereafter freely traded in and may be resold and retransferred any number of times during the eight years it may remain in bond and may be moved all over the country. It may also be bottled in bond. No provision exists for the distiller to know of its location or ownership; he is given no notice of, and has no check on, the place where stored or the means of transportation employed on removal from one bonded warehouse to another. The minority conclusion is that in all instances the distiller is primarily and ultimately liable, and that in paying the tax, the bonded warehouse pays not its own obligation, but that of the distiller. The distiller would remain primarily liable, irrespective of the cause or manner of the removal from bond. If such a liability exists, the distiller for his protection must in all instances pay the tax and sell the liquor tax paid. He

could not afford to take the risk of selling the liquor in bond and thereafter being compelled to pay in taxes many times the selling price and without right to reimbursement. This would necessarily limit the extent of manufacture and sale and would defeat the very purpose for which the internal revenue bonded warehouses were created.

(b) The provisions, diligently provided for the protection of the receiving bonded warehouse, that distilled spirits can only be transferred to a receiving bonded warehouse on its application and by a carrier designated by it, become wholly superfluous and unnecessary, and failure to afford the same or similar protection to the distiller becomes inexplicable.

(c) The conclusion is without precedent. It is in conflict with the construction of the Treasury Department charged with the enforcement of the law.¹ Such interpretation is entitled to great weight and consideration.

United States v. Philbrick, 120 U. S. 52, 59, 30 L. Ed. 559, 561.

It is likewise in conflict with two decisions of the United States Circuit Court of Appeals.

United States v. National Surety Company of Kansas City, 122 Fed. 904, 910; certiorari denied by the Supreme Court, 191 U. S. 573, 48 L. Ed. 307;

United States v. Guest, 143 Fed. 456, 459, 460.

¹For convenience, Treasury Decision 20,290 is printed in the appendix.

(d) The fact that the tax in this instance was demanded and collected by the Government from the receiving bonded warehouse and not from the distiller, is in accord with the Treasury Decision referred to. It is unreasonable to believe that it is the practice of the Government to demand and collect the tax from a party secondarily liable, and resort only to the party primarily liable after the security of the party secondarily liable has been exhausted.

CONCLUSION.

Petitioner respectfully submits that a writ of certiorari should issue.

Dated, San Francisco, California,
October 4, 1943.

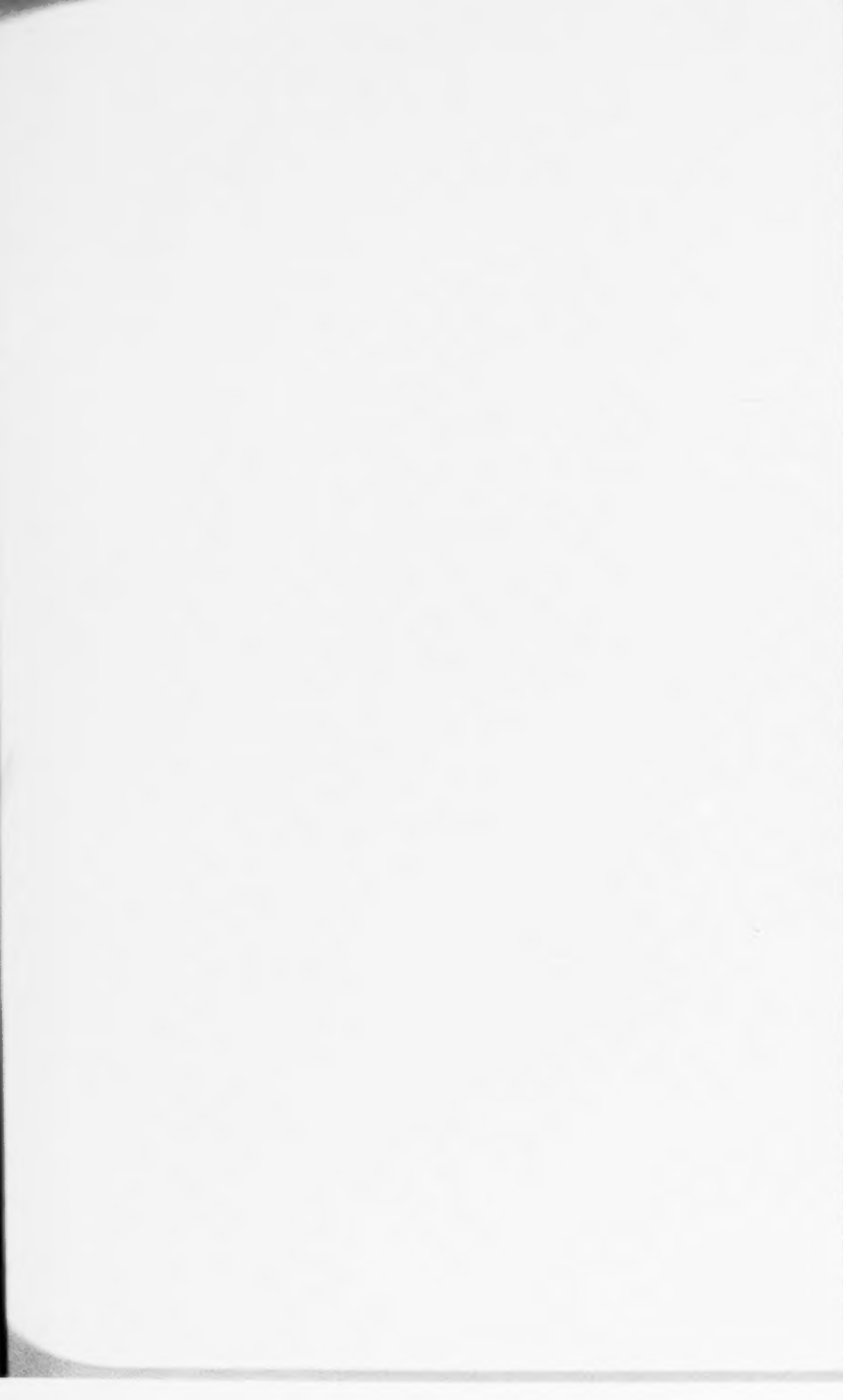
Respectfully submitted,

THEODORE H. ROCHE,

Attorney for Petitioner.

NORMAN A. EISNER,
Of Counsel.

(Appendix Follows.)





Appendix

“Treasury Decisions (1899), Vol 1:
No. 20,290

Warehousing and distillers' bonds.

Suit should be first brought on warehousing bonds to recover tax on spirits before resort is had to the distiller's bond.

Treasury Department
Office of
Commissioner of Internal Revenue
Washington, D. C., March 28, 1899.

SIR: Your letter of the 21st instant has been received, in which you inquire whether the principal and sureties on a grain distiller's bond (Form 30) are liable for the tax on distilled spirits produced under said bond and deposited in warehouse, although the tax on said spirits be covered by a warehousing bond (Form 80); and also whether suit can be brought on the distiller's bond to recover tax on spirits when the principal and surety on the warehousing bond are insolvent.

In reply, you are informed that, when it becomes necessary to institute suit for the tax on spirits covered by a warehousing bond, it should be first brought on the warehousing bond, and should the amount realized from such suit be insufficient to meet the tax, or should both principal and surety on the warehousing bond be found to be insolvent, resort may then be had to the distiller's bond (Form 30).

It may be laid down as a rule that remedy on the warehousing bond for the tax on spirits covered thereby should be exhausted before resort is had to the distiller's bond (Form 30).

Respectfully yours,

G. W. Wilson, Commissioner.

Mr. Park Agnew, Collector Sixth District, Alexandria, Va."

APPLICABLE STATUTES AND REGULATIONS.

From Internal Revenue Code

Title 26

Section 2800. TAX.

(a) RATE.

(1) DISTILLED SPIRITS GENERALLY. There shall be levied and collected on all distilled spirits (except brandy) in bond or produced in or imported into the United States an internal revenue tax at the rate of \$2.25 (and on brandy at the rate of \$2.00) on each proof gallon or wine gallon when below proof and a proportionate tax at a like rate on all fractional parts of such proof or wine gallon, to be paid by the distiller or importer when withdrawn from bond.

* * *

(b) TIME FOR PAYMENT.

(1) BONDED DISTILLED SPIRITS. For time for payment of tax on bonded distilled spirits, see paragraph (1) of subsection (a).

(2) **DISTILLED SPIRITS NOT BONDED.** The tax upon any distilled spirits, removed from the place where they were distilled and not deposited in bonded warehouse as required by law, shall, at any time within the period of limitation provided in section 3312, when knowledge of such fact is obtained by the Commissioner be assessed by him upon the distiller of the same, and returned to the collector, who shall immediately demand payment of such tax, and, upon the neglect or refusal of payment by the distiller, shall proceed to collect the same by distraint. But this provision shall not exclude any other remedy or proceeding provided by law.

* * *

(c) **TIME OF ATTACHMENT.** The tax shall attach to distilled spirits, spirits, alcohol or alcoholic spirit, within the meaning of subsection (b) of section 2809 as soon as this substance is in existence as such, whether it be subsequently separated as pure or impure spirit, or be immediately, or at any subsequent time, transferred into any other substance, either in the process of original production or by any subsequent process.

(d) **PERSONS LIABLE.** Every proprietor or possessor of, and every person in any manner interested in the use of, any still, distillery, or distilling apparatus, shall be jointly and severally liable for the taxes imposed by law on the distilled spirits produced therefrom.

(e) **LIEN.**

(1) **PROPERTY SUBJECT TO.** The tax shall be a first lien on the spirits distilled, the distillery used for distilling the same, the stills, vessels, fixtures, and tools therein, the lot or tract of land whereon the said distillery is situated, and on any building thereon from the time said spirits are in existence as such until (except as provided in paragraph (3), the said tax is paid.

* * *

Section 2814. DISTILLER'S BOND.

(a) **FORM AND APPROVAL.**

(1) **IN GENERAL.** Every person intending to commence or to continue the business of a distiller shall, on filing with the collector his notice of such intention, and before proceeding with such business, and on the 1st day of May of each succeeding year, execute a bond in the form prescribed by the Commissioner, conditioned that he shall faithfully comply with all the provisions of law relating to the duties and business of distillers, and shall pay all penalties incurred or fines imposed on him for a violation of any of the said provisions; and that he shall not suffer the lot or tract of land on which the distillery stands, or any part thereof, or any of the distilling apparatus, to be incumbered by mortgage, judgment, or other lien, during the time in which he shall carry on said business. Said bond shall be with at least two sureties, approved by the collector of the district, and for a penal sum not less than the amount of tax on the spirits that can be distilled in his distillery

during a period of fifteen days. But in no case shall the bond exceed the sum of \$100,000.

* * *

Part III. Internal Revenue Bonded Warehouses.

Section 2872. ESTABLISHMENT AND CONTROL.

The Commissioner is authorized, in his discretion, and upon the execution of such bonds as he may prescribe, to establish warehouses, to be known and designated as internal revenue bonded warehouses, to be used exclusively for the storage of spirits distilled at a registered distillery, each of which warehouses shall be in charge of a storekeeper-gauger. Every such warehouse shall be under the control of the District Supervisor of the Alcohol Tax Unit district in which such warehouse is located, and shall be in the joint custody of the storekeeper-gauger and proprietor thereof, and kept securely locked, and shall at no time be unlocked or opened or remain open except in the presence of such storekeeper-gauger or other person who may be designated to act for him. No dwelling house shall be used for such a warehouse, and no door, window, or other opening shall be made or permitted in the walls of such warehouse leading into a distillery. Such warehouses shall be under such further regulations as the Commissioner, with the approval of the Secretary, may prescribe. 53 Stat. 331.

Section 2873. REGULATIONS FOR ESTABLISHMENT,
MAINTENANCE, AND SUPERVISION.

The establishment, construction, maintenance, and supervision of internal revenue bonded warehouses shall be under such regulations as the Commissioner, with the approval of the Secretary, shall prescribe. 53 Stat. 332.

Section 2874. DISCONTINUANCE OF WAREHOUSE AND
TRANSFER OF MERCHANDISE.

(a) AUTHORIZATION. Whenever, in the opinion of the Commissioner, any internal revenue bonded warehouse is unsafe or unfit for use, or the merchandise therein is liable to loss or great wastage, he may in either such case discontinue such warehouse and require the merchandise therein to be transferred to such other warehouse as he may designate, and within such time as he may prescribe. Such transfer shall be made under the supervision of the collector, or of such other officer as may be designated by the Commissioner, and the expense thereof shall be paid by the owner of the merchandise. Whenever the owner of such merchandise fails to make such transfer within the time prescribed, or to pay the just and proper expense of such transfer, as ascertained and determined by the Commissioner, such merchandise may be seized and sold by the collector in the same manner as goods are sold upon distraint for taxes, and the proceeds of such sale shall be applied to the payment of the taxes due thereon and the cost and expenses of such sale and removal, and the balance paid over to the owner of such merchandise.

Section 2879. DEPOSITS OF SPIRITS IN WAREHOUSES.

(a) ENTRY FOR DEPOSIT. The distillers of all spirits removed to an internal revenue bonded warehouse shall enter the same for deposit to such warehouse, under such regulations as the Commissioner may prescribe. Said entry shall be in such form as the Commissioner shall prescribe.

(b) TIME FOR PAYMENT OF THE TAX. The tax on all distilled spirits hereafter entered for deposit in internal revenue bonded warehouses shall be due and payable before and at the time the same are withdrawn therefrom and within eight years from the date of the original entry for deposit therein; and warehousing bonds hereafter taken under the provisions of the internal revenue laws shall be conditioned for the payment of the tax on the spirits as specified in the entry before withdrawal from the internal revenue bonded warehouse and within eight years from the date of said entry.

(c) BOND REQUIRED. The Commissioner shall prescribe the form and penal sums of bonds covering distilled spirits in internal revenue bonded warehouses and in transit to and between such warehouses: PROVIDED, That the penal sums of such bonds covering distilled spirits shall not exceed in the aggregate \$200,000 for each such warehouse.

(d) RENEWAL OF BOND. A new bond shall be required in case of the death, insolvency, or removal of the surety or sureties, and may be required in any other contingency affecting its validity or impairing its efficiency, at the discretion of the Commissioner.

And in case the warehouseman fails or refuses to give the bond required, or to renew the same, or neglects to immediately withdraw the spirits and pay the tax thereon, or if he neglects to withdraw any bonded spirits and pay the tax thereon before the expiration of the time limited in the bond, the collector shall proceed to collect the tax by distraint, issuing his warrant of distraint for the amount of tax found to be due, as ascertained by him from the report of the storekeeper-gauger if no bond was given, or from the terms of the bond if a bond was given. But this provision shall not exclude any other remedy or proceeding provided by law.

Section 2880. WITHDRAWAL FROM WAREHOUSE AND
COLLECTION OF TAX ON SPIRITS SUBJECT TO EX-
CESSIVE LEAKAGE.

(a) POWER OF THE COMMISSIONER. If it shall appear at any time that there has been a loss of distilled spirits from any cask or other package deposited in an internal revenue bonded warehouse, other than the loss provided for in Section 2901 (b), which, in the opinion of the Commissioner, is excessive, he may instruct the district supervisor of the district in which the loss has occurred to require the withdrawal from warehouse of such distilled spirits, and direct the collector to collect the tax accrued upon the original quantity of distilled spirits entered into the warehouse in such cask or package, notwithstanding that the time specified in any bond given for the withdrawal of the spirits entered into warehouse in such cask or package has not expired. If the said tax is

not paid on demand, the collector shall report the amount due upon his next monthly list, and it shall be assessed and collected as other taxes are assessed and collected.

Section 4041. ISSUE OF INSTRUCTIONS, REGULATIONS,
AND FORMS.

(a) IN GENERAL. The Secretary shall prescribe forms of entries, oaths, bonds, and other papers, and rules and regulations, not inconsistent with law, to be used under and in execution and enforcement of the various provisions of the internal revenue laws; and he shall give such directions to collectors and prescribe such rules and forms to be observed by them as may be necessary for the proper execution of the law.

Section 407. LIQUOR TAX ADMINISTRATION ACT.

The distinction between distillery bonded warehouses, general bonded warehouses, and special bonded warehouses is hereby removed, and any warehouse for the storage of spirits distilled at a registered distillery, prior to tax-payment, shall be operated as an Internal Revenue Bonded Warehouse. The establishment, construction, maintenance, and supervision of Internal Revenue Bonded Warehouses shall be under such regulations as the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, shall prescribe.

REGULATIONS FOR INTERNAL REVENUE BONDED WAREHOUSES ISSUED BY COMMISSIONER OF INTERNAL REVENUE WITH THE APPROVAL OF THE SECRETARY OF THE TREASURY. (TAKEN FROM TREASURY DECISION 4651.)

Par. 44. The proprietor of each Internal Revenue Bonded Warehouse shall furnish transportation and warehousing bond on Form 1571 in a penal sum sufficient to cover the tax at the rate imposed by law, now or hereafter in force, on all distilled spirits to be stored in such warehouse and to be in transit thereto at any one time: Provided, That the maximum penal sum of such bond shall not exceed \$200,000 for each such warehouse: And provided further, That the proprietor of any distillery, general or special bonded warehouse established according to law and actually being used on the date of the enactment of the Liquor Tax Administration Act for the storage of distilled spirits on which the tax has not been paid, may furnish, in lieu of new bond on Form 1571, a consent of surety on Form 1533 (supplemented, if necessary, as provided in Paragraph 45 hereof), extending the terms of his existing warehousing, or transportation and warehousing, bond or bonds as the case may be, to cover the tax on distilled spirits stored in, and in transit to, the Internal Revenue Bonded Warehouse operated by him.

Par. 50. A new bond may be required at any time, in the discretion of the District Supervisor, or under instructions of the Commissioner. A new bond shall be required immediately in case of the death, removal, or insolvency of a personal surety, or insolvency of a corporate surety. Executors, administra-

tors, assignees, receivers and trustees continuing the business must execute a new bond or obtain the consent of the surety or sureties on the existing bond or bonds. When, in the opinion of the District Supervisor, the interests of the Government demand it he shall require the proprietor of an Internal Revenue Bonded Warehouse to give a new bond for an increased amount.

Par. 68. Where a new bond (Form 1571) in a penal sum sufficient to secure the tax on all distilled spirits in the internal revenue bonded warehouse and in transit thereto is filed to supersede a bond or bonds of the same or a prior series and there is no record of violation of law or regulation by the principal, the District Supervisor shall, after approval of the superseding bond, prepare Form 1490, "Notice of Bond Termination", in quadruplicate (in quintuplicate if there are two sureties), and forward the original to the Deputy Commissioner, one copy to each obligor on the bond, and retain one copy to be filed with the bond to which it relates. Where assessments have been made against the principal, the District Supervisor will not issue Form 1490 until a statement has been obtained from the Collector of Internal Revenue that such assessments have been paid.

Par. 70. Upon receipt of an application for the release of a bond (Form 1571), or of a bond of a prior series, the District Supervisor will examine his records to ascertain whether there is any outstanding liability against the bond. If and when the District Supervisor is satisfied that there is no outstanding

liability against a bond, the release of which has been applied for, he will prepare Form 1491, "Notification of Release of Bond", in quadruplicate (in quintuplicate if there are two sureties), and forward the original copy to the Deputy Commissioner, one copy to each obligor on the bond, and retain one copy to be filed with the bond to which it relates. Where an offer in compromise of civil liability or an application for remission, or claim for abatement of taxes, has been sent to the Deputy Commissioner, and notice of final action has not been received, the District Supervisor will not take any action toward the release of the bond until such notice has been received, and a statement has been obtained from the Collector of Internal Revenue that the tax involved and all outstanding assessments, if any, have been paid.

Par. 95. Distilled spirits deposited in an Internal Revenue Bonded Warehouse may be transferred in bond to another such warehouse, or withdrawn upon tax-payment, or withdrawn in bond free of tax for exportation or other lawful purposes.

Par. 102. Distilled spirits deposited in an Internal Revenue Bonded Warehouse in original packages may be transferred to another such warehouse for storage therein. Spirits deposited in storage tanks may also be so transferred in approved containers.

Par. 103. Where the transfer is to be made between bonded warehouses in the same supervisory district, the proprietor of the receiving warehouse shall execute an application for the transfer of the spirits on Part 1 of Form 236, in quadruplicate. If the spir-

its are to be drawn from storage tanks, the application will show, in addition to the other applicable data, the kind of spirits and the maximum quantity in tax-gallons to be transferred. All copies of the form will be forwarded by the applicant to the District Supervisor. If the applicant has on file a good and sufficient bond, the District Supervisor will execute Part 2 and Part 3 of the form and forward all copies to the storekeeper-gauger at the transferring warehouse.

Par. 113. Where the transfer is to be made between warehouses in different districts, the proprietor of the receiving warehouse shall file with the District Supervisor of his district an application for the transfer of the spirits on Part 1 of Form 236, in quintuplicate, in the manner indicated in paragraph 103. If the applicant has on file a good and sufficient bond, the District Supervisor will execute the certificate to that effect on Part 2, and transmit all copies to the District Supervisor of the district in which the transferring warehouse is located. The District Supervisor of such district will execute Part 3, his order to the storekeeper-gauger to gauge and release the spirits, and will then forward all copies to the storekeeper-gauger at the transferring warehouse, who will proceed as in the case of the transfer of spirits between warehouses in the same district.

Par. 118. In case the proprietor of a bonded warehouse fails or refuses to give bond as required, or to renew the same, or neglects immediately to withdraw the spirits and pay the tax thereon, or if he neglects

to withdraw any bonded spirits and pay the tax thereon before the expiration of the time limited in the bond, the collector shall proceed to collect the tax by distraint, issuing his warrant of distraint for the amount of the tax found to be due, as ascertained by him from the report of the storekeeper-gauger if no bond was given, or from the terms of the bond if a bond was given.

Par. 119. If it shall appear at any time that there has been a loss of distilled spirits from any cask or other package deposited in an Internal Revenue Bonded Warehouse, other than the loss provided for in Section 3221, R. S., as amended, which, in the opinion of the Commissioner is excessive, he may instruct the District Supervisor of the district in which the loss has occurred to require the withdrawal from warehouse of such distilled spirits, and direct the collector to collect the tax accrued upon the original quantity entered into the warehouse in such cask or package, notwithstanding that the time specified in any bond given for the withdrawal of the spirits entered into warehouse in such cask or package has not expired.

Par. 120. Whenever the owner of distilled spirits stored in any Internal Revenue Bonded Warehouse fails, upon the discontinuance of such warehouse, to transfer such spirits to such other warehouse as the Commissioner may designate, and within the time prescribed by him, or to pay the just and proper expense of such transfer, as ascertained and determined by the Commissioner, such spirits may be seized and

sold by the Collector in the same manner as goods are sold upon distraint for taxes.

Par. 130. No allowance can be made under Section 307 of the Liquor Tax Administration Act, or any other statute, for losses of distilled spirits by leakage or evaporation from railroad tank cars, or from storage tanks in a bonded warehouse, or from packages filled from such storage tanks. When a storage tank is emptied, the loss will be ascertained by the storekeeper-gauger and reported to the District Supervisor. Tax will be assessed and collected on such loss, unless the same is due to destruction by accidental fire or other casualty or to theft, and the tax remitted under Sections 3221 and 3223 R. S., or under Section 16 of the Liquor Law Repeal and Enforcement Act, respectively. When a package filled from a warehouse storage tank is withdrawn, tax will be collected on the original contents of such package unless withdrawn tax-free. If withdrawn tax-free, tax will be collected on the difference, if any, between the original gauge and the withdrawal gauge.

The foregoing regulations are taken from Treasury decision 4651 dated June 27, 1936, governing Internal Revenue Bonded Warehouses. There are in all 138 paragraphs covering details of construction, operation and control of such warehouses.



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IN THE

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CHARLES ELMORE OROPLEY
CLERK

Supreme Court of the United States

OCTOBER TERM, 1943.

No. 420

THE AMERICAN DISTILLING COMPANY,

Petitioner,

vs.

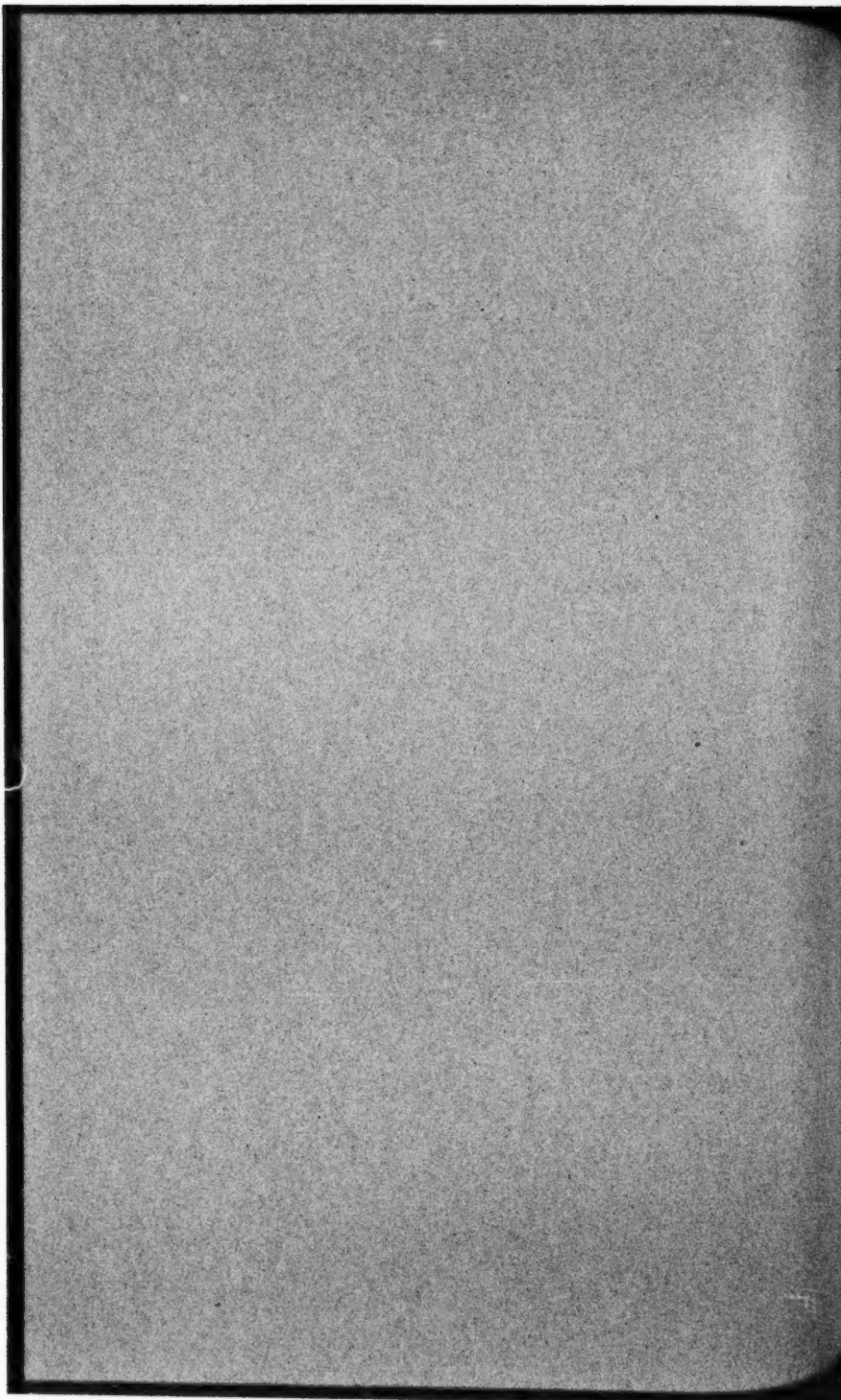
LOS ANGELES WAREHOUSE COMPANY,

Respondent.

ANSWER OF RESPONDENT TO PETITION FOR WRIT OF CERTIORARI

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THE AMERICAN DISTILLING COMPANY,

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Respondent.

ANSWER TO PETITION FOR WRIT OF
CERTIORARI.

Statement of the Case.

The statement of this case as set forth in the decision of the California Supreme Court [R. 165-167] may be accepted as a correct one inasmuch as Petitioner directs no criticism against it but contents itself with a challenge of the legal conclusions reached by both the majority and the minority opinions in Respondent's favor. Petitioner's summary and statement of the case appearing on page 2 of the Petition for Certiorari and adopted by reference on page 16 of the brief in support of the petition appears, however, to convey the impression Respondent was acting in this matter for San Angelo Corpora-

tion rather than for The American Distilling Company. Such was not the case. [R. 42-44, fols. 69-72, incl., and 47, fol. 77.] Petitioner was the *distiller* and the *owner* of the liquor, and it is nowhere claimed that San Angelo Corporation ever acquired any interest in the liquor whatsoever. Respondent had no dealings with San Angelo Corporation with respect to this lot of liquor.

The sole object of this proceeding is to place ultimate liability upon Respondent for the Government tax upon Petitioner's liquor in which Respondent had no interest whatever except as bailee.

It was in the capacity of distiller-owner that Petitioner enlisted the services of Respondent in attempting to consummate a sale to San Angelo Corporation. [R. 42-44.] Title to the liquor at all times prior to its destruction remained in Petitioner.

Rule 5 of Section 1739 of the California Civil Code provides:

"If the contract to sell requires the seller to deliver the goods to the buyer, or at a particular place, or to pay the freight or cost of transportation to the buyer, or to a particular place, the property does not pass until the goods have been delivered to the buyer or reached the place agreed upon."

Petitioner had undertaken to pay the freight to Respondent's warehouse in Los Angeles and to deliver the goods at that point. [R. 42, fol. 70.]

The fundamental question here involved is not who as between the bailor (Petitioner) and bailee (Respondent) is liable in the *first* instance to the Government for the excise tax, but as between themselves, *both* having been liable to the Government, upon which one does the ulti-

mate liability fall? Respondent does not question its liability to the Government under its warehouse bond (a special contract). It does, however, challenge as revolutionary and unsupported by reason, or justice, the contention of Petitioner that it, a mere constructive custodian of the liquor without possessing the status of either distiller, or owner, of such liquor should be charged with liability for the tax without right of reimbursement from the distiller-owner.

ARGUMENT.

The Liquor Tax Is Not Imposed Upon a Mere Custodian, But Upon the Spirits Themselves.

Section 2800(a)(1) of the Internal Revenue Code* provides:

"There shall be levied and collected on all distilled spirits (except brandy) in bond or produced in or imported into the United States an internal revenue tax at the rate of \$2.25 (and on brandy at the rate of \$2.00) on each proof gallon or wine gallon when below proof and a proportionate tax at a like rate on all fractional parts of such proof or wine gallon, to be paid by the distiller or importer when withdrawn from bond." (Emphasis ours.)

Section 2800(c) of the Internal Revenue Code provides:

"The tax shall attach to distilled spirits, spirits, alcohol or alcoholic spirit, within the meaning of subsection (b) of section 2809 as soon as this substance is in existence as such, whether it be subsequently

*All references are to Chapter 26.

separated as pure or impure spirit, or be immediately, or at any subsequent time, transferred into any other substance, either in the process of original production or by any subsequent process." (Emphasis ours.)

Section 2800(d) of the Internal Revenue Code provides as follows:

"Every proprietor or possessor of, and every person in any manner interested in the use of, any still, distillery, or distilling apparatus, shall be *jointly and severally* liable for the taxes imposed by law *on the distilled spirits* produced therefrom." (Emphasis ours.)

Section 2800(e)(1) of the Internal Revenue Code establishes a lien as follows:

"The tax shall be a first lien on the spirits distilled, the distillery used for distilling the same, the stills, vessels, fixtures, and tools therein, the lot or tract of land whereon the said distillery is situated, and on any building thereon from the time said spirits are in existence as such *until* (except as provided in paragraph (3)), *the said tax is paid.*" (Emphasis ours.)

There is nothing in any one of those provisions of the Internal Revenue Code which even suggests that a warehouseman as such is liable for the tax. His liability in so far as the Government is concerned springs from his special contract with the Government—his transportation and warehousing bond—required by paragraph 44, T. D. No. 4651, approved June 27, 1936. (Appendix to Petition P. X.)

The duty of the distiller to pay the tax is not extinguished by the warehousing bond but the warehousing bond is *cumulative* and *additional* security which the Government demands and receives whenever the distiller obtains a delay in the payment of the tax through the storing of the liquor in a bonded warehouse.

United States v. National Surety Co., 122 Fed. 904, 909-910;

United States v. Richardson, 127 Fed. 893.

If the contention of Petitioner is correct, all a distiller or owner need do to shift the burden of the tax is to deposit the liquor in a bonded warehouse and such a deposit *ipso facto* relieve the distiller, or owner from further liability for the tax. Such an exemption was never contemplated by the law as clearly appears from the sections of the Internal Revenue Code above referred to and the cases cited. This unique contention made by Petitioner is commented upon by the decision in the District Court of Appeal in the following language [R. 163]:

"If defendant is correct in its contention that as between it and the receiving warehouse the primary and ultimate responsibility is upon the receiving warehouse, and it, as between it and the receiving warehouse, is not liable, it would mean that a distiller-owner could store distilled spirits in the bonded warehouse of another and leave it there so stored for over eight years. The receiving warehouse would have to pay the tax at the end of eight years, and thereafter, if defendant is correct, the distiller-owner could remove the spirits from bond without paying or refunding the tax to the custodian warehouse. If

defendant is correct, the distiller would be completely and forever free from liability once the spirits passed into the hands of a bonded warehouse. That is not the law. (*San Angelo, etc. v. S. End W. Co.*, 19 Cal. App. (2d) (Supp.) 749; *American D. Co. v. Hollywood S. Co.*, 28 Cal. App. (2d) 439.)

From the above analysis it follows that as between the receiving warehouse and the distiller the ultimate and fundamental responsibility rests upon the distiller. The tax is not imposed on custody, but on the spirits themselves, and those spirits were distilled by defendant. When plaintiff paid the tax, as it was required to do, it was not paying its debt, but the debt of defendant. Plaintiff's primary responsibility to the government for the tax was simply the result of Congress' attempt to facilitate the administration of the tax provisions, and the collection of the tax. The liability is ultimately imposed on the distiller-owner, and not on the temporary custodian of the liquor."

We respectfully submit that the foregoing quotation is a correct interpretation of the law.

As Between Petitioner and Respondent the Petitioner's Liability Is Primary.

Section 2800(a)(1) and (d) of the Internal Revenue Code provides for this primary liability, and the following cases tend to support that proposition.

Germania Fire Ins. Co. v. Thompson, 95 U. S. 547, 24 L. Ed. 487;

Harkins v. Williard, 146 Fed. 703, 706;

Greenbrier Dist. Co. v. Johnson, 88 Fed. 638.

Also appropriate to the occasion is the language of this Court in the case of *Farrell v. United States*, 99 U. S. 221, 25 L. Ed. 321, where it is said, in holding the distiller liable for the tax:

“Depositing distiller spirits in a government warehouse did not make them the property of the Government, or cause them to be held at the risk of the bailee. The property remained in the distiller, and the risk of loss by fire or any other casualty was, consequently, his.”

The statement contained in the petition, at page 10, to the effect that the warehouseman assumed the obligation for the tax “as a condition to the privilege of operating as such” is clearly inconsistent, we think, with the cases of *United States v. National Surety Co.*, *supra*, and *United States v. Richardson*, *supra*, holding that the warehousing bond does not extinguish the distiller's debt but that it is additional and cumulative security for the payment of that debt.

Another unsound premise relied upon by Petitioner is found on page 10 of its petition where it states:

“The *owner* cannot obtain possession without payment of the tax. It is, however, quite a different matter to be obliged to pay the tax without getting the liquor.” (Emphasis of the word “owner” ours.)

The destruction of the liquor in the case at bar was tantamount to its removal from bond by its owner. Such was the effect of the decision of the California Supreme Court [R. 169, fol. 255] and it finds support in *Farrell v. United States*, 99 U. S. 221, 25 L. Ed. 321, where the Court determined that the destruction of the liquor by a fire in a bonded warehouse was a removal of the liquor

therefrom and the tax had to be paid by the distiller and owner. Section 2800(a)(1) of the Internal Revenue Code states that the tax shall be paid by the *distiller* when the liquor is withdrawn from bond. Here the distiller and owner are one and the same.

We, therefore, do not think it a misconception of the law to assert that the last above mentioned quotation from the petition really amounts to a confession by Petitioner that the owner is liable for the tax, and should be compelled to pay it to Respondent here.

None of the Four Errors Specified in the Brief of Petitioner Is Tenable.

We find on page 16 of the petition and brief in support thereof the alleged errors claimed by Petitioner, the first of which is that the California Supreme Court erred in holding the federal tax on distilled spirits to be a property tax.

Some confusion appears to have arisen in the mind of Petitioner as to the sense in which the majority opinion of the California Supreme Court has used the expression following [R. 169]:

“So far as persons dealing with the liquor are concerned the tax follows the property as a necessarily included part of the value thereof”

suggested, perhaps, by what is said in the minority opinion [R. 169-170]. It appears to us that the majority opinion has construed the liquor tax in the sense that this Court construed the tobacco tax in *Patton v. Brady*, 184 U. S. 608, 46 L. Ed. 719, where it is said:

“it is not a tax on property as such, but upon certain kinds of property, having reference to their origin and their intended use,”

and in harmony with the case of *Hedger v. Union Ins Co.*, 17 Fed. 498, 499, where the Court held the entire value of the whiskey included the tax thereon.

Section 2800(a)(1), (b)(2), (c), (d), and (e)(1) of the Internal Revenue Code all indicate quite clearly, we think, that the tax is on the *goods* themselves, and Section 2800(e)(1) specifically provides that the tax shall be a first lien upon the spirits distilled from the time they come into existence, as such, until the tax is paid without exception. The tax thus follows the property, as the majority opinion holds, and the value of the owner's interest in the liquor is made up of the liquor as such plus the amount of the tax.

The second specification of error is that the California Supreme Court erred in holding the owner personally liable for the payment of the tax as an incident of ownership. What the court really said was that it becomes an obligation of the owner as an incident of ownership to pay the tax on removal from bond. [R. 169.] In effect Petitioner conceded this to be true when it said, on page 10 of the petition:

"The owner cannot obtain possession without payment of the tax."

Petitioner advances no reason why a bailee-warehouseman should pay the tax except that it is a burden he assumes for the privilege of doing business as such, which is contrary to the holding in *United States v. National Surety Co.*, *supra*, stating the warehousing bond is given as additional security only, does not extinguish the distiller's obligation to pay the tax and is required and given pursuant the Government's comprehensive system of administration and collection of liquor taxes. No statute

or other authority is cited to the effect that a stranger to the title or manufacture of distilled spirits is liable for the tax except in the instance of the bonded warehouseman who gives additional security in the form of his transportation and warehousing bond and thereby assumes liability under a special contract which is in no manner designed to relieve the distiller-owner in this case from the payment of his debt.

The third specification of error states the California Supreme Court erred in holding Petitioner-bailor liable to Respondent-bailee for the amount of the taxes advanced by the latter. The trial court found as follows [R. 47, fol. 77]:

“That each and all of said sums so advanced and expended by the Plaintiff were paid out in pursuance of the authority and instructions of the Defendant given to the Plaintiff to bring about a transfer of said gin to Plaintiff’s said warehouse in Los Angeles, California, and said payments were the direct consequence of acts done by Plaintiff at the direction of the Defendant and were in each instance paid in Defendant’s behalf and for Defendant’s benefit.”

and as follows [R. 48, fol. 79]:

“It is true that within two (2) years last past, in the County of Los Angeles, State of California, at the special instance and request of the Defendant, the Plaintiff furnished and paid out to and for the use and benefit of Defendant the sum of five thousand fifteen and 14/100 (\$5,015.14) dollars which Defendant then and there impliedly agreed to repay to plaintiff on demand with legal interest.”

As a basis of Respondent's right of recovery against Petitioner we cite Section 27 of Act 9059, 2 Deering's General Laws, 1937, page 4218, which provides:

"Subject to the provisions of section 30, a warehouseman shall have a lien on goods deposited by the owner or by the legal possessor of the property or on the proceeds thereof in his hands, for all lawful charges for storage and preservation of the goods, also for all lawful claims for money advanced, interest, insurance, transportation, labor, weighing, cooperating and other charges and expenses in relation to such goods; also for all reasonable charges and expenses for notice, and advertisements of sale, and for sale of the goods where default has been made in satisfying the warehouseman's lien."

California Civil Code, Section 1856, similarly provides:

"A depositary for hire has a lien for storage charges and for advances and insurance incurred at the request of the bailor, and for money necessarily expended in and about the care, preservation and keeping of the property stored, and he also has a lien for money advanced at the request of the bailor, to discharge a prior lien, and for the expenses of a sale where default has been made in satisfying a valid lien. The rights of the depositary for hire to such lien are regulated by the title on liens."

In the case of *San Angelo Wine & Spirits Corp. v. South End Warehouse Co.*, 19 Cal. App. (2d) (Supp.) 749, it was held that a warehouseman had a lien upon the liquor concerning which he had paid the excise taxes.

See also:

American Dist. Co. v. Hollywood Storage Co., 28 Cal. App. (2d) 439, 82 P. (2d) 711.

In the case at bar Respondent could not assert a lien against the liquor since it was destroyed, but Section 32 of Act 9059, 2 Deering's General Laws, 1937, page 4218, provides:

"Whether a warehouseman has or has not a lien upon the goods, he is entitled to all remedies allowed by law to a creditor against his debtor, for the collection from the depositor of all charges and advances which the depositor has expressly or impliedly contracted with the warehouseman to pay."

The correctness of the decision of the California Supreme Court in view of the foregoing authorities is unchallengeable, we think.

Under the authorities heretofore cited it sufficiently appears that it was the debt of The American Distilling Company that was paid by Los Angeles Warehouse Company and under the state law the latter was entitled to reimbursement.

The fourth and last specification of error is to the effect that the California Supreme Court erred in holding Petitioner liable to Respondent for the *amount* of the liquor excise taxes.

Here again the short answer to that purported criticism is that it was Petitioner's debt as distiller-owner, in the final analysis, which was paid by Respondent and Respondent was entitled to recover for the aggregate of the amounts it had advanced in behalf of and for the benefit of Petitioner upon the authorities cited in both the majority and minority opinions of the California Supreme Court, and for the reasons therein and herein stated.

Petitioner's Contention That the California Supreme Court Decision Is in Conflict With Federal Laws Is Untenable and No Federal Question Is Here Involved.

It is argued by Petitioner on page 21 of its brief in support of the petition that Treasury Decision 20, 290, and the two cases of *United States v. National Surety Co.*, 122 Fed. 904, and *United States v. Guest*, 143 Fed. 456, conflict with the California Court's decision, but that cannot be true because no such question as here concerns us was involved in either of those cases or discussed in the Treasury Decision referred to. In each and all of those cited instances the Government's legal rights were discussed and decided in controversies between the Government on the one hand and the taxpayer on the other. No question was there involved as to the ultimate liability between a distiller-owner and a warehouseman. Such a question is not the concern of the Government, and it does not presume to define nor determine the respective rights and liabilities of those two parties. Such a question involves state law alone, does not present a federal question, and must be resolved in the light of state statutes and decisions, and that is what the California courts have done.

Petitioner argued his theory of applicability of the *National Surety Company* case, *supra*, and the *Guest* case, *supra*, as well as Treasury Decision No. 20290, to both the California District Court of Appeal and the Supreme Court of California and in each without avail simply be-

cause the correct analyses of those two federal cases and the Treasury Decision reveal their applicable limitations to the policy and rights of the Government in proceedings instituted *by the Government* for the collection of excise taxes on spirits due the Government only.

We therefore disagree with the statement contained on page 8 of the petition that a state court has decided a federal question of substance not theretofore determined by this Court, and assert that what the state court really decided was a question of ultimate liability as between two citizens of the State of California, one a bailor, and the other a bailee, both of whom were primarily liable to the Government for an excise liquor tax, and which tax the Government had proceeded to collect from the bailee in pursuance of its plan to facilitate the administration of internal revenue tax provisions and the collection of the tax.

The federal laws and regulations governing the imposition and the method of the collection of the tax do not determine the rights and liabilities of the parties to this litigation as between themselves once the tax has been paid.

The state law under such circumstances must be looked to and applied for such purposes, and that is what has been done in this case.

"The lack of substantiality in a federal question may appear either because it is obviously without merit or because its unsoundness so clearly results from the previous decisions of this court as to foreclose the subject." (*California Water Service Co. v. Redding*, 304 U. S. 252, 255.)

For the reasons hereinabove stated and because of the legal authorities herein cited it is contended by Respondent that the petition for a writ of certiorari to the Supreme Court of the State of California should be denied.

Dated at Los Angeles, California, October 30, 1943.

Respectfully submitted,

ALLEN W. ASHBURN,

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SHERMAN ANDERSON,

Of Counsel.